FRANCHISES OR MONOPOLIES—THEIR PUBLIC OWNERSHIP AND OPERATION.

In the agitation about a public ownership—federal, state or municipal—of telegraph lines, railroads, lighting plants and similar enterprises essential to modern society, there are two sets of extremists. One group urges the public ownership and conduct of all corporate business charged with what, in legal phrase, has been termed a "public use." The other group favors private enterprise exclusively; and the limitation of governmental functions to the old fashioned administration of state, federal and town laws as designed by our American grandfathers. But "new occasions teach new duties: time makes ancient good uncouth." The contrast is political as well as mechanical between the days of the saddle-bag-mail courier, and the long-distance telephone. Imagine, in the interest of local traffic in firewood and vegetables, partisans of free trade and protection dividing over a prohibitory duty by the Empire State (1787) against the cargoes of Connecticut and New Jersey bumboats. It seems odd, too, that more than a generation later so wise a jurist as Judge Story should write in his "Commentaries" that the Post Office establishment was fraught with dangers to our civic welfare because it was "susceptible of abuse to an alarming degree." He declared that "the whole correspondence of the country is so completely submitted to the fidelity and integrity of the agents who conduct it, and the means of making it subservient to mere state policy are so abundant, that the only surprise is that it has not already awakened the public jealousy, and been placed under more effectual control. It may be said without the slightest disparagement to any officer who has presided over it, that *if ever the people are to be corrupted or their liberties are to be prostrated, this establishment will furnish the most facile means*

and be the earliest employed to accomplish such a purpose" (Story on Constitution, Sec. 1536). It is within the science of government to utilize the progressive achievements of modern life with the least modicum of human friction; and if possible without injustice. The two extremes of government doing everything, and government doing nothing except securing life, liberty and property, are now discarded, as well by the theorist and trained politician, as by the common judgment of the people.

A Starting Point.

Notwithstanding the pronounced political difference in relation to governmental ownership or management of franchise properties, on one point, and one only, is there a general consensus of opinion; and that is *where a public concession is given on which a business is consequently more or less grounded, there, a public compensation shall be rendered, and a public supervision shall be exercised.*

It seems strange to us to-day that this latter proposition should ever have been challenged. It is as old as the English common law. Yet, less than twenty years ago, in what is reckoned as the most independent, if not the most intelligent political community in the country, it was the issue of a bitter contest that raged in the Empire State regarding the indiscriminate discrimination by railroads, and the efforts in establishing the present harmless railroad commission.

Even the right to regulate charges for public services by corporations enjoying public monopolies was, strange to say, not only fiercely combatted in the legislature, when, for instance, against violent opposition, the two-cents-per-mile rate was imposed upon the New York Central Railroad; but afterward in the courts throughout the country in every stage of litigation, until the United States Supreme Court, by its decisions reiterated the principle, ancient and unassailable, that when "*property is devoted to a public use, it is subject to public regulation.*"

Chief Justice Waite declared that the limitation of the rate of charges for services rendered in a public employment, or for the use of property in which the public has an interest, established no new principle of law, but only gives effect to an old one. He said "Where the common law prevails, it has been customary from time immemorial for the legislature to declare what shall be a reasonable compensation" for a public service; or perhaps more properly speaking to fix a "maximum beyond which any charge would be *un*reasonable." . . . "We know the power may be abused; but that is no argument against its existence. For protection against abuses by legislatures the people must resort to the polls, not to the courts" (*See Munn* v. *Illinois*, *94 U. S. Reports*, *130*). This is a power, as the late Mr. Justice Miller of the same court declared, which "extends to the protection of the lives, limbs, health, comfort and quiet of all persons, and to the protection of all property within the state: . . . . and persons and property are subjected to all kinds of restraint and burdens in order to secure the general comfort, health and prosperity of the state" (16 Wall. 62).

Apart from government ownership and management several modes of securing the public interest have been adopted. Sometimes it has been by regulating public charges; sometimes by attempting to prescribe the modes and times of public service; or by exercising more or less control over the service, through public officials like federal, state or municipal boards; sometimes by requiring periodical payments in return for a franchise; and in some instances by its absolute sale for a price paid.

Regulating Charges not an Adequate Supervision.

But the general public is not satisfied simply with regulating rates. That is a matter which in the nature of things is surrounded by too many conditions, dependent and variable,

to be fairly secured by men not experts. Nor can it be insured by competition where competition is impossible. All that seems to be practicable in this direction from day to day is attained when obvious extortion is prevented.

The possibility of extortion excites the passions of cupidity, of envy, and of reckless enmity. If the franchise unfortunately shall have been granted in perpetuity, those interested will discover abundant argument why its operation, management or ownership should not be disturbed. If, because of legal complications, its terms cannot be modified, then undoubtedly such public regulations may be superimposed, as will secure the best and most approved service that sound judgment, exercised in the public interest, may reasonably require. There are few instances where the most negligent corporate sinner may not thus be disciplined, with the result of an improved public service.

When a franchise has been leased or is being paid for, nominally or actually, it has been found in practice very difficult to control its relations to the public. For instance, the simple matter of requiring chain guards and gates for our New York ferries, operated under leases from the city, was the outcome of many demands and contests. Even where there was no other public concession than the inevitable monopoly attending the right of eminent domain and the running of a railroad, improvements, for instance, required by the public interests were not made in the equipments and facilities of the great New York Central system, until the facilities and example of the competing Pennsylvania system had justified the public criticisms and put to shame the wealth-producing New York nerve-vein.

The Sale of a Franchise.

Franchise sales are likely to receive fresh illustrations from our new island possessions. The Insular Commission appointed by the War Department to examine into the affairs of Porto Rico recently reported among their

recommendations that "all concessions should be granted only after proper advertisement in the newspapers in Porto Rico and the United States: and then sold to the highest bidder at public sale." In municipal affairs generally, franchise sales find many advocates.

The popular notion that a public franchise should be sold for what it is worth, is replete, if not with error, at least with misfortunes. The so-called "business man," another name for a horseless jockey, a man looking for a "going concern" to ride in,—is usually noisy about what such and such a franchise ought to be worth, or what he would give for it, or what it ought to bring, paralyzing the innocent by his marshaling of estimates with imaginary statistics.

Such a sale is a gamble for the purchaser, and a worse gamble for the public, who constitute the seller, but who are generally "sold!" It may be right for an earl to sell at auction (if he would be so foolish) the hunting franchise on his estates; for royalty to sell a tobacco monopoly for all that can be had for it; for the king to sell his special privileges, ferries, highway tolls, the right to manufacture liquors, or to dispense them, with more or less monopoly, in certain places. But it is an intrusion on the fundamental doctrines of republican government to part absolutely with any of the serious functions of government; such as the right to tax for essentials—and water supply, light supply, electric supply and transportation supply have become modern necessities. Such an intrusion becomes invidious and dangerous to liberty, civic equality and social order, when distinguished by a consideration paid by the favored party.

It is either in acknowledgment of this wrong, or else a perpetuation of it, that the present charter of Greater New York prohibits the granting of public franchises for a longer period than twenty-five years, with a right to renewal. This implies that the franchise *may* be granted absolutely for that length of time. The *un*wisdom of this provision is in

permitting the interested public to remain financially *un*interested for *any* period of time. The wisdom of it is in prohibiting the perpetuation of a franchise. The gamble, to be sure, is "a very little one," with a sort of "limit" to the game.

The propriety of any such "game," whether its territorial limitation be city, state or nation, may well be doubted. Still, it must be conceded that the imperative provisions in the New York charter looking toward the public ownership, and option of management, of the entire property and franchise at the end of twenty-five or fifty years, are big steps in the right direction; although the wide latitude of official discretion permitted in deferring the possible public ownership is upon principle open to many objections.

It may be said that private capital to exploit a public improvement will not be forthcoming unless the project be financially attractive, and that its attraction must consist in the payments by the public for service rendered. This may be granted. The franchise given should render such service until the capital shall be repaid or secured, together with a suitable profit for the investment and for the risks of the venture. But should it go beyond this; should it offer an opportunity for amassing extortionate riches? More cannot be demanded than a suitable public service, even at the cost and risk if necessary of public ownership.

Where the conditions are not financially attractive to private capital—as is sometimes the case regarding great canals, or water works for supplying great cities—the public credit and the public purse may become essential. For illustration, the Erie Canal, the Pacific Railroads, the Sault Ste. Marie Canal, and other great lake and river waterways: This may also be the case regarding the great rapid transit necessities on Manhattan Island, but not necessarily.

Where private capital is probable it will look out for its own security and reward; and this just security and liberal reward it is in the public interest to invite and to maintain.

How Shall Franchises be Paid For?

Perhaps it is in deference to considerations of this character that absolute franchises have heretofore been granted in return for annual payments out of earnings, gross or net. Such devices, however, have usually proved unsatisfactory; as really they are, and should be, for they are only species of gambling. Both sides are then playing a sort of "blind" game, followed by a crop of annual law suits as to who is entitled to the stakes.

Where then is the line to be drawn? What shall be the measure, if any, of a direct public financial interest—if not absolute ownership—in those public franchises which depend for their earnings on the contributions of the multitudes for public services rendered by the franchise owners?

Theoretically the answer is a simple one, although concededly difficult of practical application in many cases.

The answer is to be found in such an immediate *partial interest as*, with the accretions, if there be great profits, will *gradually absorb the private capital;* but if there be no profits will leave the great public represented and jointly interested with the private capital employed in working out the financial and public salvation or condemnation of the enterprise.

To illustrate: If the franchise, a street railroad, for instance, is to be granted to a corporation by or for the benefit of a city, suppose a fourth or other fraction of the stock should be issued, let us assume for the franchise, the dividends on this fraction of stock to be utilized for the purchase of more outstanding stock, to be purchased of the lowest bidder offering it; and all of the stock issued to be subject to the public right of purchase at a fixed premium. The ordinary rights of a stockholder, reinforced by a prescribed representation among the directors, and official visitation, would insure scrutiny over the management, and afford some reasonable guarantee to investing stockholders, as well as to the utilizing public.

The premium say at 110, 125 or 150, and the limitation coupled with an assurance of dividends, say at 6, 8 or 10 per cent, would furnish attraction for ordinary capital. The laws of New York, fairly applied, would operate to prevent excessive capitalization; while provision could easily be made against bonds, prohibiting them if necessary, or permitting them within suitable limitations.

Should the franchise prove excessively profitable the official holdings would gradually accumulate. They could then, with the same or with larger reservations, be sold again, a sort of partial refranchise sale, to the highest bidder; or half of the holdings sold. The management would thus remain in private hands, but under official surveillance, and in the actual direction of representatives of the shareholders of the capital invested.

Should the franchise prove unprofitable the public purse may be invited to give aid, if worthy of it and if public advances may be duly authorized. If all ends in failure there is the ordinary process of dissolution, receivership and possibly reorganization.

At all events, the mutual initial object is attained in the attempted venture with security to capital, and with due regard to the present and future interest of the community to be served.

How About Old Monopolies?

Well, some one observes, that device of partial public ownership and representation may be made applicable to future enterprises, but not to existing corporations. Possibly so. Yet there are few public corporations affected with a "public use," or enjoying a public franchise (unless it be extortionately profitable), whose shareholders would not be gratified to have an assured premium fixed for their limited dividend paying shares—and all stock of franchise monopolies should be limited in dividends.

If the stock be selling at a low figure, and be not on a

dividend paying basis, it would require slender inducement to persuade the shareholders to surrender a fraction of their holdings for the establishment of such a partial public ownership as would be equivalent to a sinking fund and guaranteed profit. I admit the practical difficulties in a case like a street railway, or gas company, whose shares are quoted at, say, two hundred or upwards. Yet even such a case might yield to fair "treatment."

The power creating and regulating a corporation operating a public monopoly may reasonably be exercised to secure improved public conditions by way of investment, as well as in improved service.

Over fifty years ago, when ten per cent was the legal limitation of dividends, it was the policy of New York railroad law that the excess of profits should go toward reducing fares. An ancient specimen enactment toward limitation of profits was afforded in another instance where the tracks were laid with the old "flat bar rail," which it was desired should be superseded by the "fifty-six pounds" to the "lineal yard" rail. So the Legislature of 1847 restricted the dividends to *three* per cent, and directed the earnings in excess to "constitute a sinking fund," to be used for no other purpose except to replace the old with the described new rail; and prescribed a *penalty of forfeiture of charter if the substitution was not made* anyhow within three years from the passage of the law.

Limitation of dividends and the application of excess of profits toward reduction of public charges, or in some other form for the benefit of the general public, even to the payment of the excess directly into the public treasury, is no novel proposition or policy. As applied to many corporations affected with a "public use" it is a well-established public policy, fairly applicable according to the circumstances of each case.

Of course the contrivances of a profitable corporation to evade a profitable showing, and to apply its actual profits to

extravagance, or to what is in truth a further capitalization, or to what properly belongs to "capital" account and not to the ordinary expenses, or even to a fair rate for extraordinary repairs and maintenance, is and always will be a contest not limited simply to a question of bookkeeping; but an issue that is cropping up in every great enterprise between good faith and wrong doing; between a good motive and a perverse motive. Thus it might be argued that the official holdings would never be increased.

But allowing for the honest and ignorant differences in judgment there is always a point in the finances of every current business where the distinctive line between a profitable or an unprofitable business may readily be drawn by one who has the authority to draw it. The present laws and officials and courts of justice are quite adequate to right any serious error in drawing square financial lines respecting the operations of New York corporations.

True, many apparently absurd reports are to-day required; but when it comes to distinguishing between profits and losses, and capital and expenses—and these are the true exhibits of the cost of production or service—there is little need for legislation to enable the courts or officials to set out the truth touching the financial operations of public corporations responsible to the authorities of the Empire State. Financial jugglery, and an occasional dishonest official, will scarcely defeat a well-defined public policy once fastened by law to a public trust. Profit, or the absence of profit, is easily proven. Here is an illustration:

How Cost of Gas in New York was Once Shown.

The first New York legislative investigation of monopolies that ever arrived, or perhaps attempted to arrive, at the actual cost of production, or of service rendered, was the famous Gas Investigation of 1886.

The Senate Committee was met at the outset by the proffer of the gas companies to furnish their own figures showing

their estimated cost of gas, but with objections to the committee's experts examining all their books; the companies claiming to be only private corporations, selling gas to the city among other consumers. Of course this claim was not legally tenable, although it had been otherwise assumed by the authorities and by the public for a generation.

The committee, however, upon finally securing the books of all the gas companies then operating in New York City, quietly surprised the companies by figuring out the original investments, the yearly expenditures of a permanent character, and for current service, the aggregate receipts from customers, the aggregate annual productions, the aggregate purchases of materials, the totals of investments, sales, and annual dividends; and thus by inexorable mathematics announced to every gas company in New York, what until then had never been stated, even among the managers, namely, the actual capital paid in and employed, and the actual cost of each thousand feet of gas as delivered to customers, for every year each gas company had been doing business.

No such corporate showing was ever made respecting a New York monopoly; and no better demonstration was ever made that the actual cost of service, cost of product to a customer, consists in distinguishing capital investment from current expenses, and in arriving at the real profits of the monopoly, or real losses as thus distinguished for an annual or other fairly selected period.

The cost of gas being thus shown for each and every "plant" in operation with relation to the increasing population in the city, the legislature promptly enacted some ill-considered laws decreasing and regulating the price of gas; and has renewed such laws to the present time.

No such comprehensive and philosophical work relating to municipal monopolies was ever accomplished by any legislative committee; although the progressive laws it recommended were not passed.

No New Scheme.

Nor does the possible or actual public ownership, if happily it should sometimes result from the accumulated accretions of the sinking fund capital, present any new feature of public policy. It is enough at present to trace it back to the charter of the first railroad built in this state before the first general railroad law. It is a feature found in all the special railroad charters up to as well as including the first general railroad law, under which railroad corporations were organized in New York. By all these enactments it was in substance provided that the railroad properties might vest in and become the property of the state upon the repayment to the railroad company of the amount expended for construction and permanent fixtures, and the actual value of the cars, engines, machinery, chattels and real property in its use, with interest on such sums at a rate not less than 10 per cent per annum, together with all moneys expended for repairs, etc., after deducting the amount received for tolls, freights and passage money. It is no part of this paper to discuss whether this feature of law is still in force. Suffice it to say, that while in the opinion of some it is, the legislature in the exercise of the state's right of eminent domain may nevertheless reach a corresponding result by making adequate provision at any time for vesting in the state the franchises, fixtures, property and appurtenances of its railroads therein. At all events a charter is seldom encountered that may not be revoked, and such terms as public policy may dictate may be laid down by the state for renewing in some other form, or upon some other conditions, the public service already being rendered by a public corporation; subject to proper compensation for property or property rights that may be extinguished.

Valuations.

An incidental question arises as to the standard by which valuations for public purposes shall be measured. Shall

they be based on the actual cash capital invested plus a proper interest; or shall they be based on the earning power as shown by the statistics of receipts and disbursements; or shall they be based at what would be the cost to duplicate the system? No one of these three standards is false for its special and legitimate purposes. The great industrial combinations, through their corporate securities as offered to and extensively dealt in by the public, are at the present time furnishing the investing public with large conundrums under these three classes of inquiries; and every answer will depend chiefly on the standpoint of the questioner, and on the motive of both the question and the answer.

If the public ownership of a great corporation, as a live "going concern," is to be assumed, the legislature or the courts, or both, will readily answer such questions according to the circumstances of each case. But, if it is only a question as to what shall be the charge to the public for service rendered, the public can be trusted in the future, as it has demonstrated by its conduct in the past, to deal fairly, and even liberally with corporate capital employed in the operation of franchise monopolies.

What difference does it make to the consumer if a product is manufactured at a less cost by private than by public management, if the difference goes into the treasury of a private corporation, instead of going to reduce charges or to increase the proportion of public ownership?

The Proportion of Ownership.

The fundamental question then, in carrying forward this policy of fractional ownership and future absorption and resale (whether the franchise monopoly be an old one or a new one), relates to the initial fraction of shareholding to be conceded in any particular case. Shall it be one-third, one-quarter, fifth or tenth? Shall the fraction be for cash, or for the franchise? In these days of stock issues by the

millions for so-called "good will," "secret processes," patents and other intangible assets, there would seem to be little or no difficulty in securing for the official holdings an adequate and appropriate fraction.

Cities having the disposal or control of franchises might in many instances require legislation to carry forward a policy of this nature. If so, there would be no serious difficulty in securing the necessary legislation. In many instances no further state enactments would be requisite.

A Bill Once Introduced.

There is one instance of a proposed law on these lines that, by way of illustration, may be mentioned in this connection. In 1881, there was introduced into the New York Legislature a bill to amend the general railroad laws of New York, so as to provide for state partial ownership and future absorption. This bill specially applied to railroad corporations which should thereafter be incorporated, or result from consolidation or reorganizations. Provision was made, however, that existing corporations, by delivering to the controller proportionate stock and filing proper certifications and acceptances of the act, might voluntarily come within its provisions. Some reorganizations then going forward were considering the acceptance of such provisions, or voluntarily adopting them as part of their fundamental organization, with a view to the permanent stability of their securities to be issued.

There was attraction to the financial eye in the compulsory sinking fund feature and assured purchase at a premium if the enterprise should progress to a reasonable dividend. The bill, however, was never discussed owing to the factional strife that overwhelmed all other subjects, and to the partisan warfare that convulsed the legislature of that year.

The principles of the bill, however, and the methods of their application on the foregoing plan are clear and simple, and easily worked out for application to any locality, or for

any public corporation. Any good lawyer will readily map out the essential details for application of the system to any proposed public work, or for any special locality.

Incidental Considerations.

Of course there is a large mass of considerations that will crop up for more or less attention. The population and character of the territory to be served; the initial cost of construction, of equipment, and the cost of its efficient maintenance; the amount of charges practicable, or in expectancy, upon the public; the quality of service; the integrity of stock issues; the honesty and ability of management, the possible competition, or variation in public demands and facilities, the private property or damages to be paid for in the establishment and conduct of what may be termed the "plant" by which the franchise is to be operated—are each and all signal factors in the problem. But while requiring due attention they are as brushwood for removal to expose the central factor, namely, the initial fraction of capital stock to be dedicated to the public ownership.

That question is to be settled according to the exigencies of each case, and not by any rule of thumb. It must be settled, not by any general law, but be the outcome in each instance of judgment, guess-work, prophetic vision and agreement. Once settle whether the fraction shall be a fifth, a third, a quarter, or a half, and all other details fall without difficulty into their proper sphere for solution.

Rapid Transit Corporations.

The objectionable and philosophically erroneous proposal to grant a perpetual franchise for an underground rapid transit company in New York City may find ameliorating conditions in this plan of initial fractional ownership. In such great works the public purse or credit may legitimately purchase by instalments, if need be, initial fractional holdings, in whole or in part. Thus the question of a

constitutional debt limit need not be encountered in any such public work while inviting private investment to aid it.

Conclusion.

It is not claimed that this method of financing will solve the complex rapid transit question for Greater New York; but it is claimed that, unless public franchises are to be owned and operated by the people and their chosen officials, there is no fairer method yet proposed to secure to the people that reasonable share of profit which is their due from the control and operation of a valuable franchise.

Such franchises grow in value with their use, and with the natural increase in population, and in improved modern facilities. It is the perpetration of a wrong to give away such franchises; and the wrong is imperceptibly lessened by such a grant for an assumed consideration. It remains nevertheless, a continuing wrong, fostering bad blood and industrial sores incurable by the ballot, and inciting social explosions. An absolute sale, an irretrievable alienation of a public franchise is fundamentally wrong.

It may be in line with Spanish Imperialism; but it is unrepublican. In a republic a sale, if franchise sale there be, should be of *a concession for the shortest time* possible prior to an approaching public resumption and ownership of the whole franchise and property, together with the *largest fractional public ownership meanwhile* that competing capital will profitably allow. Under a republican form of government the consideration for a franchise should *not* be a payment to the present generation for a yoke upon its successors.

The competition should be for the *shortest period bidder*, or for the *smallest fractional bidder, or both.*

The object of the sale should be to invite private capital into the matter for the shortest time possible, and upon the smallest fractional interest in the enterprise that will be adequate to redeem the capital with its suitable profits.

Governor Pingree, of Michigan, is quoted as saying (and he might wisely have said it) that "Good municipal government is an impossibility while valuable franchises are to be had and can be obtained by corrupt use of money in bribing public servants."

Of course the larger the initial fraction of public ownership, the larger would be the official representation in the Board of Directors. It will be said that this enforced representation in the Board of Directors being at first in a hopeless minority, will afford no real protection to the public. An answer is obvious.

Disinterested and able men will always be found to accept such useful and honorable public stations. Their reports, and the common knowledge of the doings of a public corporation subject to such official scrutiny, and to such visitation as is common to banks, insurance companies and other institutions of public trust, will not admit of continued jugglery or of systematic wrongdoings.

The laws of the state are quite adequate to protect even the minority shareholder, if his knowledge is equal to his legal weapons. Moreover it would be easy to reinforce those laws, if need be, in their applicability to corporations in which the public is a joint owner.

Tossing to and fro all the diverse considerations in favor of and against public ownership of corporations enjoying a public franchise, the opinion is ventured—at least for the purpose of provoking useful discussion—that a joint public ownership, coupled with such an interest as, if valuable, will contingently increase to the point of ultimate absorption of entire ownership, furnishes a philosophical and presently practical line for the concession and operation of franchises and monopolies.

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